

Message Text

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SUBJECT: BORDER TAX ADJUSTMENTS IN THE EUROPEAN COMMUNITY

REF: MTN GENEVA 8714

1. WE SHARE MTN GENEVA'S JUDGMENT THE EUROPEAN COMMUNITY WILL REFUSE TO NEGOTIATE A FUNDAMENTAL REVISION OF THE GATT BORDER TAX ADJUSTMENT RULES. A SERIOUS US EFFORT TO MAKE SUCH REVISIONS PART OF THE SUBSIDY/COUNTERVAILING DUTY EXERCISE WILL PROBABLY WRECK THE CHANCE OF THE US GETTING IMPROVEMENTS IN INTERNATIONAL EXPORT SUBSIDY PRACTICES.

2. OVER THE PAST 12 YEARS, DURING FOUR US ADMINISTRATIONS, THE UNITED STATES HAS CONDUCTED TWO MAJOR BUT FUTILE CAMPAIGNS ON THE BORDER TAX ISSUE. IN BOTH THE OECD EXERCISE OF
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1963-68 AND THE GATT EXERCISE OF 1968-70 THE EUROPEAN COMMUNI-

TY HAS BEEN TOTALLY OPPOSED TO SUGGESTIONS FOR A MAJOR REVISION IN THE BORDER TAX ADJUSTMENT RULES. THE RECENT STEEL COUNTERVAILING DUTY CASE SHOWED ONCE MORE THE VIRULENT EUROPEAN REACTION TO ANY CLAIM THAT THE FULL REMISSION OF THE TVA ON EXPORTS AMOUNTS TO A SUBSIDY.

3. THE STRENGTH OF THE EUROPEANS' SENTIMENT ON THE BORDER TAX ISSUE STEMS FROM THEIR BELIEF THAT THE CURRENT SYSTEM OF BORDER ADJUSTMENTS FOR INDIRECT TAXES IS THE ONLY PRACTICAL AND ECONOMICALLY THEORETICALLY DEFENSIBLE WAY TO HANDLE INTERNAL TAXES IN EXPORT TRADE. THEY BELIEVE IT IS POLITICALLY IMPOSSIBLE AND UNFAIR TO DOMESTIC COMPETITORS TO CHARGE LOWER TAXES ON IMPORTS THAN ON DOMESTIC GOODS. THEY SEE THEMSELVES AS EXTRAORDINARILY DEPENDENT UPON WORLD TRADE, I.E., ON BEING COMPETITIVE IN EXPORTS. THEY BELIEVE THAT THEIR AGREEMENT TO A SYSTEM OF SIGNIFICANTLY LESS THAN FULL REMISSION ON EXPORTS WOULD SO CRIPPLE THEIR COMPETITIVITY IN WORLD MARKETS THAT THEY WOULD BE FORCED TO SIGNIFICANTLY ALTER THEIR CURRENT INDIRECT TAX SYSTEM-A MAJOR FORM OF GOVERNMENT REVENUE AND A KEY ECONOMIC POLICY TOOL. IN THEIR VIEW, A NEGOTIATION WHICH RESULTED IN SOME FORM OF FREEZING OF BORDER TAX ADJUSTMENTS WOULD EFFECTIVELY DEPRIVE EUROPEAN GOVERNMENTS OF THE ABILITY TO CHANGE THEIR RATES OF INDIRECT TAXES. THEIR JEALOUSY ABOUT MAINTAINING NATIONAL SOVEREIGNTY ON THE RATES AND COVERAGE OF THE TVA HAS SO FAR EFFECTIVELY FRUSTRATED EUROPEAN COMMUNITY EFFORTS TO MAKE THE TAX SYSTEMS AND TAX RATES COMMON IN THE MEMBER STATES.

4. THEY DO NOT BELIEVE THAT THE UNITED STATES WOULD BE ABLE TO PARTICIPATE IN A SYSTEM OF LESS THAN FULL BORDER TAX REMISSION ON EXPORTS SINCE THEY SERIOUSLY DOUBT THAT THE FEDERAL GOVERNMENT COULD FORCE STATES TO COLLECT RETAIL SALES TAXES ON SHIPMENTS ABROAD OTHER THAN BY A FEDERAL TAX ON EXPORTS, WHICH THEY NOTE IS UNCONSTITUTIONAL. THEY ADD THAT EVEN IF THE US SHOULD CHARGE INDIRECT TAXES ON ITS EXPORTS, THEY WOULD HAVE A HARD TIME JUSTIFYING A SYSTEM WHICH WOULD MEAN, IN EFFECT, THAT THEIR CONSUMERS HAD TO PAY TAXES TO THE UNITED STATES GOVERNMENT ON PRODUCTS IMPORTED FROM THE UNITED STATES.

5. THE EUROPEANS CLAIM THAT A LIMIT ON BORDER ADJUSTMENTS FOR INDIRECT TAXES WOULD CAUSE A RISE IN THEIR EXPORT PRICES AND LIMITED OFFICIAL USE

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A FALL IN THEIR IMPORT PRICES AND AMOUNT TO A REVALUATION OF THEIR CURRENCIES AGAINST THE DOLLAR, A DEVELOPMENT WHICH THEY WOULD STOUTLY RESIST, PARTICULARLY DURING A PERIOD WHEN THEY ARE COLLECTIVELY RUNNING A LARGE TRADE DEFICIT WITH THE US.

6. IN SUM THE MISSION BELIEVES THAT IF THE UNITED STATES UNDERTAKES A MAJOR EFFORT TO REVISE THE BORDER TAX ADJUSTMENT RULES, IT SHOULD DO SO IN FULL RECOGNITION OF THE FACT THAT THE

EUROPEANS WILL NOT AGREE. CONSEQUENTLY SUCH AN EFFORT WOULD BE
LIKELY TO UNDERCUT THE ENTIRE SUBSIDY/COUNTERVAILING DUTY
EXERCISE.MORRIS

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